

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter Of)	
)	
Jurisdictional Separations Reform)	CC Docket No. 80-286
And Referral to the Federal-State)	
Joint Board)	DA 00-1865

Comments of John Staurulakis, Inc.

John Staurulakis, Inc. (JSI), hereby files comments in response to the Federal Communications Commission's (Commission's) *Public Notice*¹ regarding the July 21, 2000, *Recommended Decision* by the Federal State Joint Board (Joint Board) on Separations Reform.² JSI is a consulting firm specializing in financial, regulatory and management services to approximately 200 incumbent local exchange carriers (ILECs) throughout the United States. JSI assists these ILECs in the preparation and submission of jurisdictional cost studies and Universal Service Fund (USF) data to the National Exchange Carrier Association (NECA), and routinely prepares and files tariffs with the Commission on behalf of a number of these

¹ Recommended Decision Issued by Federal-State Joint Board on Jurisdictional Separations, CC Docket No. 80-286, Public Notice, DA 00-1865 (Public Notice), August 15, 2000.

² Jurisdictional Separations Reform and Referral to the Federal-State Joint Board, CC Docket No. 80-286, *Recommended Decision*, July 21, 2000.

ILECs. In that the proposals and questions raised in the *Public Notice* will affect the jurisdictional cost recovery of its client companies, JSI is an interested party in this proceeding.

The Public Notice invites comment on the Joint Board's recommended decision that the Commission institute a five-year freeze of all Part 36 category relationships and allocation factors for price cap carriers, and a freeze of the allocation factors for rate-of-return carriers. The Joint Board further recommended that the freeze be based on a carrier's data from the twelve months prior to the issuance of an order by the Commission on the Recommended Decision and that the freeze be mandatory and apply to all carriers subject to the Commission's Part 36 rules. Moreover, the Commission seeks comment regarding the Joint Board's recommended decision to freeze the local dial equipment minutes (DEM) factor. The recommendation for the local DEM factor is to freeze it at some substantial portion of the current year level based on data from the twelve months preceding the implementation of the freeze, should the Commission find that Internet traffic is jurisdictionally interstate in the proceeding that has been initiated as a result of the remand by the United States Court of Appeals for the D.C. Circuit on the Commission's Reciprocal Compensation Ruling. Finally, the Commission seeks comment on the precise level of the reduction in the local DEM warranted in light of any effects that Internet usage has had on jurisdictional allocations or consumers.

Overall, JSI is in agreement with the Joint Board's recommended decision to freeze separations factors for rate-of-return carriers. Despite its overall agreement, JSI recommends the following technical and policy considerations associated with a freeze of separations factors: (1) Internet usage should immediately be excluded from the development of the frozen local DEM factor; (2) all usage-sensitive factors should be adjusted to exclude the impact of Internet usage before being frozen; (3) factors from a company's most recent interstate cost study as submitted

to NECA should form the basis of the factors to be frozen; (4) adjustments to frozen factors should be allowed during the five-year period for exogenous changes; (5) average schedule companies converting to cost should be allowed to establish frozen factors based on actual use and excluding Internet usage; and (6) for acquisitions and mergers, frozen factors of the newly acquired property should be combined with frozen factors of the existing property using a weighted average of access lines.

I. INTERNET USAGE SHOULD IMMEDIATELY BE EXCLUDED FROM THE DEVELOPMENT OF THE FROZEN LOCAL DEM FACTOR

The primary objective for implementation of a five-year freeze of all allocation factors according to the Joint Board is to “provide much needed simplification and stability to the separations process in a time of rapid market and technology changes.” As the Commission and the rest of the telecommunications industry have already recognized, one of the primary reasons for the instability in the current jurisdictional allocation process is the impact that Internet usage is having on interstate allocation factors. Since current settlement procedures require that Internet usage be treated as intrastate (local) traffic for rate-of-return carriers, the impact of ever-increasing amounts of Internet usage is to reduce the percent of interstate allocation that rate-of-return carriers utilize to allocate levels of investments and expenses to the interstate jurisdiction. As a result, many LECs that participate in the NECA pooling process have been experiencing a shift in their jurisdictional revenue requirements from interstate to intrastate.³

³ Letter from Richard A. Askoff (NECA) to Lawrence E. Strickling (FCC), Oct. 5, 1999. “NECA projects, based on results of a recent data request to its member companies, that approximately 18 percent of 1998 local/intrastate dial equipment minutes represent Internet traffic. Treating this jurisdictionally interstate traffic as intrastate for separations purposes produces a \$170 million misallocation of costs to the state jurisdiction for NECA pool members.”

As JSI has stated in previous comments⁴, Internet-related usage should be extracted from the development of jurisdictional allocation factors. JSI's position regarding dial-up Internet traffic is consistent with the Joint Board's Recommended Decision. However, where the Joint Board suggests the exclusion of Internet usage before freezing the local DEM factor only if and when the Commission determines that Internet usage is interstate in nature, JSI believes that there should be no such qualification for the following reasons.

First, it is very clear that current Commission as well as Congressional policy is to preclude the assessment of any type of access charge upon Internet Service Providers (ISP). Therefore, it could be months, if not years, before the Commission renders a decision with respect to the jurisdictional nature of dial-up Internet usage. JSI suggests that where actual amounts of Internet usage have been measured and determined by a rate-of-return LEC, the minutes should be immediately excluded from the local DEM and the current year unweighted interstate DEM should be recalculated and frozen. Without the immediate exclusion of Internet minutes from the local DEM, many rate-of-return carriers will have frozen factors that reflect substantial amounts of Internet usage in the local DEM, creating a shift in revenue requirement from interstate to the intrastate jurisdiction thereby threatening the affordability of existing basic local service rates in rural communities and forcing the end user customer to continue subsidizing the ISP industry.

Second, the exclusion of Internet minutes prior to a Commission decision regarding jurisdiction will not assign minutes of use to the interstate jurisdiction. The Joint Board does not make the recommendation to *add* Internet usage to interstate minutes of use prior to the freezing of the DEM factors. It appears to JSI that the Joint Board recommends that Internet-related minutes of use be excluded from total local DEM minutes (using actual amounts or a default

⁴ JSI comments in CC Docket No. 80-286, In the Matter of Jurisdictional Separations Reform And Referral to the Federal-State Joint Board, DA 99-414, March 30, 1999.

percentage) prior to the freezing of factors which will automatically cause the interstate DEM factor to increase since the local DEM and therefore total DEM related minutes will decrease. However, the resulting increase in the interstate DEM factor created by excluding Internet-related usage will not be nearly as high as it would be if such usage was in turn, added to the interstate minutes of use. At this time, JSI is not suggesting that the Internet minutes previously included in the local DEM be added to the interstate minutes. However, should the Commission ultimately adopt its previous position that Internet usage is mostly interstate in nature, then JSI believes that any frozen factors should be restated to reflect Internet usage as interstate.

Finally, JSI believes that where actual measurement is not feasible, the default estimate of 95 percent suggested by the Joint Board for the freezing of the local DEM is inadequate. Should LECs be unable to accurately measure the level of Internet usage throughout their service territory, JSI recommends that a default percent representing 80 percent of the local DEM be utilized instead of the 95 percent level recommended by the Joint Board. JSI bases its recommendation on results from the 1999 study conducted by NECA⁵ that determined the level of Internet usage contained in the 1998 intrastate DEM factors for pooling member LECs to be approximately 18 percent. Using a conservative compounded annual growth rate of 10 percent, the level of Internet usage for the year 2000 would exceed 20 percent for the NECA companies.

II. ALL USAGE-SENSITIVE FACTORS SHOULD BE ADJUSTED TO EXCLUDE THE IMPACT OF INTERNET USAGE BEFORE BEING FROZEN

In addition to the local DEM factor, JSI recommends that all usage-based factors be adjusted to exclude the impact of Internet usage before being frozen. Such factors would include, for example, the subscriber line minutes of use (SLU) and the host-remote minutes of use factor.

⁵ See NECA 1999 Internet Usage Data Request, June 4, 1999.

Like the local DEM factor, all other usage-based factors should be restated to exclude Internet usage as measured or reflect a default percentage representing 80 percent of local usage.

JSI also recommends that the weighted DEM component making up the local switching support calculation for every LEC be restated to exclude any Internet usage included in the local DEM factor when the frozen component was first determined. Since usage from 1996 was utilized to derive the frozen interstate DEM component, JSI recommends that a 5 percent default factor be utilized to reduce the local DEM for 1996 and the frozen interstate component be restated accordingly. JSI suggests the use of a small default percentage since the amount of Internet usage back in 1996 was considerably less than levels being experienced today.

III. FACTORS FROM A COMPANY'S LATEST INTERSTATE COST STUDY SHOULD BE FROZEN

In the Recommended Decision, the Joint Board suggests that the Commission adopt a freeze based on a carrier's data from the twelve months prior to the issuance of an order. JSI maintains that adopting such a policy will place an unnecessary burden on rate-of-return carriers since most companies conduct calendar year studies in order to determine their interstate settlements. In the alternative, JSI recommends that any freeze adopted by the Commission be based on factors utilized in the company's most recent annual cost study submitted to NECA.

IV. ADJUSTMENTS TO FROZEN FACTORS SHOULD BE ALLOWED DURING THE FIVE-YEAR PERIOD FOR EXOGENOUS CHANGES

Contrary to the Joint Board's Recommended Decision, JSI believes that adjustments to frozen factors should be permitted during the five-year freeze period. For instance, any action taken by the Commission that results in the classification of Internet usage as interstate should result in the ability for LECs to restate their frozen interstate DEM factors and any other affected usage-sensitive factors. Moreover, for example, should existing broadband-related services such

as DSL and any future services result in a significant amount of Internet traffic being removed from the public switched network, rate-of-return carriers should be allowed to petition the Commission in an effort to restate their frozen factors.

V. AVERAGE SCHEDULE COMPANIES CONVERTING TO COST SHOULD BE PERMITTED TO ESTABLISH USAGE-SENSITIVE FACTORS AND EXCLUDE THE IMPACT OF INTERNET

For average schedule companies converting to cost, subsequent to the implementation of a separations factor freeze, the Commission should grant such companies the opportunity to establish all required factors based on the most recent calendar year data. The factors established will then be frozen for the remaining freeze period. In establishing usage-sensitive factors, especially the local DEM and the frozen, weighted interstate DEM, average schedule companies converting to cost should be required to measure the level of Internet usage and exclude this usage when establishing the local and interstate DEM factors. In the event that the appropriate level of Internet usage cannot be measured, a default factor of 80 percent of the local DEM should be utilized in establishing the frozen factors. Consistent with the suggested treatment of Internet usage for cost companies, average schedule companies converting to cost should not have to await a decision by the Commission regarding the jurisdictional nature of Internet traffic in order to exclude it from the development of frozen factors.

The implications of including Internet usage in the intrastate (local) usage-sensitive factors for average schedule LECs looking to convert to cost is significant. In completing a cost feasibility analysis for two average schedule LECs (representing approximately 22,500 access lines) in the past several months, JSI notes that the level of dial-up Internet usage as a component of total local usage was approximately 54 percent. In developing the annual interstate revenue requirement for the companies, the combined interstate revenue requirement was approximately

\$4.5 million with Internet usage excluded entirely from the development of the usage-sensitive factors, and approximately \$4 million with Internet usage included as local (as currently required by NECA). The combined difference of \$500,000 or \$1.85 per access line per month makes it extremely difficult for such companies to convert to cost, thereby denying them an opportunity to recover their costs.

VI. FOR ACQUISITIONS AND MERGERS, FROZEN FACTORS OF THE NEWLY ACQUIRED PROPERTY SHOULD BE COMBINED WITH THOSE OF THE EXISTING PROPERTY USING A WEIGHTED AVERAGE OF ACCESS LINES

When a rate of return LEC acquires exchanges from another rate of return or price-cap LEC, JSI recommends that the frozen factors of the newly acquired property be combined with those of the existing property using a weighted average of access lines. For the acquisition of exchanges by a newly created entity, the existing factors would be utilized. In the event that a rate of return LEC purchases exchanges from a price-cap LEC (and obtains the necessary price-cap waiver), category relationships would need to be unfrozen, consistent with the rate of return LEC's existing property.

VII. CONCLUSION

The detrimental impact that Internet usage is having on the jurisdictional allocations for rate of return carriers continues to increase. As a result, JSI supports a freeze of all usage-sensitive allocation factors utilizing factors from a LEC's most recent cost study as submitted to NECA. Any freeze adopted by the Commission should enable all affected LECs to immediately exclude the impact of Internet usage in establishing the frozen local DEM based on either actual recorded Internet usage or a default percent of 80 percent of local usage. Moreover, LECs should be given the opportunity to restate the frozen weighted interstate DEM component (the local switching support factor based on 1996 data) to immediately exclude any identifiable

Internet usage or utilize a default factor of 95 percent of local usage. JSI recommends that the Commission allow LECs to recalculate and refreeze all usage-sensitive factors should the Commission decide that Internet usage is interstate in nature by allowing LECs to add the amount of Internet usage previously excluded from the local DEM to the interstate DEM. JSI recommends that any company wishing to convert from the interstate average schedules to a cost basis of settlement be allowed to establish frozen factors utilizing the most recent calendar year data and excluding all Internet usage based on either actual measurement or a default factor of 80 percent of local usage. Finally, JSI recommends that rate of return LECs purchasing exchanges from other LECs develop combined frozen factors based on a weighted average of access lines of the existing and newly acquired property.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Emmanuel Staurulakis, do hereby certify that on this 25th day of September, 2000, a copy of the foregoing "Comments of John Staurulakis, Inc.", were mailed first class, postage prepaid, to the individuals listed below.

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